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No. 86-1593

In The Supreme Court Of The United States

October Term, 1986

Shell Oil Company,

Appellant

vs.

Department of Revenue,
State of Florida,

Appellee

Appeal

from the Supreme Court of Florida

Appellant's Reply Brief

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Reply

This Reply is written to focus the issue posed by Shell's Jurisdictional Statement and the Department of Revenue's motion to dismiss or affirm.

The Department has devoted an unusually large amount of its motion to matters which have not been raised by Shell and are not in controversy in this proceeding. Over one-half of the Department's motion is used to discuss income apportionment, whether Florida has properly applied federal income tax concepts against Shell, and if some of Shell's sales of oil and gas were consummated on the outer Continental Shelf ("OCS"). The Court should not be deceived or confused by these irrelevancies.

One issue alone is presented for the Court's review. That issue is whether the unambiguous declaration of Congress that "state taxation laws shall not apply to the

outer Continental Shelf"[1] is to be given any effect whatsoever. Six, short questions will frame that issue.

The answers to these six questions will demonstrate that Florida has ignored the eleven word proscription of Congress, has thwarted Congress' intended effect, and has in fact imposed its state taxation law "to the outer Continental Shelf."

1. Does Shell perform activities of an economic nature on the OCS? Of course it does, and the Department does not say otherwise.

2. Does the federal government derive an economic benefit from Shell's activities? Yes, it derives a direct economic benefit

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1 43 U.S.C. §1333(a)(2)(1972). See Appendix 9 to Shell's Jurisdictional Statement.

in the form of lease OCS royalties. The Department does not suggest otherwise.

3. Are those benefits to the federal government adversely affected by what Florida has done through its state income tax law? Of course they are, and the Department does not suggest otherwise.

4. Did Congress intend by section 1333(a)(2) to prevent state tax laws from creating adverse economic effects on federal revenues from OCS properties? Of course it did.

Ordinary statutory construction rules apply here. By applying those rules, it is plain as day that Shell's taxation by Florida is preempted by the OCS Act. The intention of a statute is primarily determined by examining the words chosen by Congress. Congress wrote: "State taxation laws shall not apply to the outer Continental Shelf." Those words are

unambiguous. Congress spoke as plainly as words can possibly be framed.

The legislative history of this eleven word formulation, moreover, is consistent with its evident meaning. Congress intended to bar all forms of state taxation, both direct and indirect. See Shell's Jurisdictional Statement at pages 15-17. The Department does not argue for a different statutory meaning or intent. It simply assumes the unstated position that an income tax levy on Shell is neither a direct or an indirect tax affecting OCS because Congress meant to ban only severance-type taxes. By this means, the Department simply ignores the very real economic impact which occurs through a reduction of lease revenues due to state tax burdens placed on OCS lease bidders.

That is, by hiding behind the federal income tax concept of "realization" to

suggest that OCS production income is a phantom or non-existent type of economic revenue, the Department and the Supreme Court of Florida mask the taxation of OCS production income by subsuming it into subsequent sales which in fact encapsulate that income. This approach ignores the entire history of the federal ban on state taxation of outer Continental Shelf properties. (See Shell's Jurisdictional Statement at pp. 14-19 and Appendix 1 at pp. 1-21 through 1-27).

Nor does the Department's and the Florida Supreme Court's superficial treatment of this issue, using realization to block analysis, address the preemptive rationale of the federal ban. The federal statute reflects a resolution of twenty seven years of debate as to whether state tax laws of any type, whether directly or indirectly imposed, should be allowed to impact federal lease revenues. In responding to

Shell's Jurisdictional Statement, the Department blithely ignores this rationale for the eleven word prohibition. (See Shell's Jurisdictional Statement at pp. 15-16, 19-21).

Shell submits that the words "state taxation laws shall not apply to the outer Continental Shelf" have a meaning that is not difficult to construe. It is easy to demonstrate that the Florida Supreme Court has held the state's income tax laws in fact do "apply" to the OCS. Shell excluded from its taxable income reported to Florida all production income derived from OCS properties, computed in accordance with the same methodology used for computing lease revenues to the federal government and for other relevant, federal income tax computations. The Department added the production income back into Shell's income for Florida tax purposes. The Florida Supreme Court upheld the inclusion of that

income. It could not be more plain that Florida taxation laws are being made to "apply" to the Shelf in each year that Shell's income is taxed in Florida.

The prohibition against the application of state tax laws to the OCS must mean that OCS income is to be disregarded in computing state taxes, or the OCS Act will mean nothing. In Maryland v. Louisiana, 451 U.S. 725 (1981), the Court implied that it would require Shell's OCS income to be disregarded by Florida in computing its income tax. The Court clearly indicated in that case that it would consider the application of state income tax laws to OCS income to be in violation of the OCS Act. The only reasonable way for Florida to conform to the OCS Act is to exclude OCS production income in computing Shell's state income tax burdens.

5. Did Shell raise and preserve the issue of federal preemption in this

proceeding? It is undisputed that Shell raised sections 1333(a)(2) and (3) of the Outer Continental Shelf Lands Act as a bar to the taxation of Shell's OCS production income in its Florida tax returns, at every phase of administrative and court proceedings in this case, and before the Florida Supreme Court.

6. Did the Supreme Court of Florida pass on the issue squarely? Yes. The Florida Supreme Court ruled squarely on the issue which Shell has asked the Court to review:

> . . . Shell contends that the time and location of the actual sale are irrelevant because no sale of OCS production can ever be subject to state taxation. Shell claims that section 1333(a)(3) of the outer Continental Shelf Lands Act supports this contention . . . . We find that Shell's reliance on section 1333(a)(3) is misplaced.

Shell Oil Company v. Department of Revenue, 496 So.2d 789, 790 (Fla. 1986), reproduced in Appendix 1 to Shell's Jurisdictional

Statement on page 1-9.) See also the dissenting opinion of Chief Justice Boyd in that case, in which Justice Shaw concurred, which asserts in detailed analysis why the OCS Act prohibits Florida from taxing OCS production income. (Appendix 1 at pp. 1-18 through 1-36).

Six simple, affirmative answers to the six, key questions prove that the issue posed by Shell in this proceeding is ripe for the Court's review. Other points raised by Shell, which are neither addressed nor controverted by the Department, demonstrate why the Court should accept review.

Shell has described this Court's continuing solicitude for congressional intent with respect to the outer Continental Shelf. (Shell's Jurisdictional Statement at pp. 17-19). Shell has described the expanding endeavors of the various states to impose their own

apportioned state income taxes on production income and thereby erode federal revenues from OCS leases. (Shell's Jurisdictional Statement at pp. 21-23). The Department's silence on these matters speaks loudly of its hope that the Court will ignore states' efforts to thwart congressional will as expressed in the eleven words of section 1333(a)(2).

The Court should not permit this to occur. The Court should accept this case for plenary review and reject the Department's request to have this appeal dismissed or affirmed.

Respectfully submitted,

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